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SUBJECT: Stabilization Measures for Pakistan's Falling Stock Market

Summary

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[1](#)1. (SBU) After consulting with the Karachi Stock Exchange Board (KSE), the Securities and Exchange Commission of Pakistan (SECP) announced measures to stabilize the stock market. These measures include: a ban on short selling to stop speculation; use of bank guarantees as security deposits; changes in the limits individual stocks may gain and lose in one day; and establishment of a USD 439 million (Rs.30 billion) stock market stabilization fund. According to the SECP, these measures are short term and will be reviewed in a month. Adnan Afridi, KSE Managing Director, told Economic Counselor that he was "very reluctant to tinker with the market." End summary.

SECP and KSE agree on market stabilization measures

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[1](#)2. (U) The Securities and Exchange Commission of Pakistan (SECP) officials and the Board of Directors and Management of the Karachi Stock Exchange (KSE) decided to adopt market stabilization measures to stop the continuing drop in KSE-listed stocks and to ensure that trading continues smoothly.

[1](#)3. (SBU) Effective June 24, the maximum drop in a daily stock price has been reduced from five to one per cent; if it loses more than one percent, trading is suspended for that stock until the following day. Similarly, the maximum daily increase of a stock price has been raised from five to ten percent; if the stock rises above this level, trading is suspended for that stock until the following day. These measures will stay in place for 30 days, and be reviewed on July 15.

[1](#)4. (SBU) Adnan Afridi, KSE Managing Director, told Economic Counselor that investors were having problems covering five percent losses on an almost daily basis. Acknowledging that "he hates tinkering with the market" and that "we waited as long as we could to implement market controls," Afridi commented that he had spoken to the London and New York exchanges prior to the imposition of these measures.

[1](#)5. (SBU) Selling shares without owning them (short selling) is now completely prohibited in the deliverable future contract market. SECP officials commented that brokers had been engaging in short selling, further driving down the market. This measure is temporary and will be reviewed at the end of July.

16. (SBU) Bank guarantees from top-rated banks are now allowed as security deposits, which must be maintained by brokers and share dealers as a financial cushion for market fluctuations. Afridi told us that the margin calls were increasing markedly, causing liquidity problems for share holders. As a result, bank guarantees have been allowed as security deposits.

17. (SBU) A USD 439 million (Rs. 30 billion) market stabilization fund will be established. Utilization of the fund will be automatically triggered in the event of extreme market volatility. SECP officials are considering buying those stocks whose prices are decreasing. Details of how the fund will operate are still under discussion, according to officials at both the SECP and KSE.

Comment

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18. (SBU) Comment: The decision to let the stock prices rise 10 percent above the previous day closing price and fall just 1 percent below the closing price is designed to give an artificial boost to the market. As a result, volumes have increased again. However, these measures have not stopped the continued drop in the market, with the exception of one or two days. Afridi was encouraged that market volumes have increased since the June 23 implementation of these measures. In their absence, the market would have registered even greater losses. The ban on short selling is likely to curb speculation. The ability to use bank guarantees for margin calls is further evidence of the effects of Pakistan's tight monetary policy

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and decreased liquidity due to a sharp drop in portfolio investment inflows. As much of the international investment in the KSE has pulled out -- at least for now -- it is the local investors which need to cover their margins in a falling market. End comment.

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